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RABAT -- PLEASE PASS TO TREASURY DAS LOEVINGER

TREASURY FOR IA - MMILLS AND RADKINS

STATE FOR EB/IFD AND EUR/SE

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SUBJECT: Scenesetter for Treasury DAS Loevinger

1. (SBU) Summary: Your visit to Turkey comes at a bumpy period in the bilateral relationship, in large measure connected with developments in Iraq. It is also a delicate moment in relations with both the IMF and EU. This message provides a brief overview of the state of bilateral relations, cooperation in Iraq, Turkey's EU accession prospects and the state of play with the IMF and EU. End Summary.

The Bilateral Relationship

2. (SBU) Bilateral relations have entered another choppy period. The Turks are freely criticizing U.S. policy in Iraq and elsewhere in the Middle East, but do not offer constructive alternatives. A barrage of media disinformation about Falluja and U.S. actions in general in Iraq -- fanned by statements by PM Erdogan and by Foreign Minister Gul alleging excessive use of force and civilian casualties -- is creating negative public opinion. Some observers have characterized the general attitude in Turkey toward the U.S. and our role in the world as the most negative in memory.

Iraq

3. (SBU) Turkey shares our goals for Iraq: a secure and stable, democratic country, united and territorially whole. To that end, Turkey has provided valuable assistance and cooperation. Ankara offered to send troops to Iraq, approved the use of Incirlik Air Base for tankers to refuel aircraft on support missions for both Operation Enduring Freedom (OEF) and Operation Iraqi Freedom (OIF), authorized the transit of US troops from Iraq, and permitted the transit of supplies for our forces and humanitarian goods. Turkey is also active in reconstruction efforts, including providing electricity for Iraq and training Iraqi diplomats, and has offered senior military leadership training in Turkey as its contribution to NATO's Iraq training mission.

4. (SBU) This cooperation is provided despite the fact that our actions in Iraq are highly unpopular with the Turkish public. Many Turks in and out of government worry about the fragility of Iraq's territorial integrity, fearing that the Kurds in the north aspire for independence and that the tensions between Sunni and Shia Arabs might become intractable. The Turks have gone on record supporting the IIG and full participation in elections, which they want to see move forward by January's end.

5. (SBU) More recently, the rising number of Turkish truckers abducted and executed in Iraq has raised concerns among the public and Turkish officials. To address this issue, the first trilateral US/GOT/IIG talks on security in Iraq were held on November 30.

6. (SBU) On Iraq debt, despite our demarches, the GOT has not articulated its position. Lower level officials and Governor Serdengecti have expressed reluctance to provide forgiveness, claiming poverty, however, we have yet to get an official reply endorsed by senior Government officials. As far as we are aware, the issue was not discussed at Secretary Snow's recent meeting with Minister Babacan in Berlin.

Counter-Terrorism/Non-Proliferation

7. (SBU) The Turks have been an active partner on other fronts in the global war on terrorism and international security: our militaries coordinate on a range of security and counter-terrorism issues, Ankara has been

supportive of international efforts to press Iran to meet its commitments to the IAEA. Turkey will again assume the command of ISAF in Afghanistan in February for a six-month period during which they will significantly increase their contribution to this important NATO mission.

18. (SBU) Turkey's regime to combat money laundering and the financing of terrorism is quite weak. A combination of technical weakness, poor interagency coordination, and inadequate attention from government leaders has stalled efforts to upgrade the legal framework or to vigorously cooperate internationally. A recent FINCEN mission found that Turkey not in compliance with some FATF recommendations and considered that Turkey would not qualify to get into the Egmont Group if it had to apply today. The FBI and DOJ are currently providing training programs on investigating and prosecuting financial crime cases and post continues to press GOT officials to beef up its anti-financial crimes regime.

EU Accession -----

19. (SBU) The European Commission in its October 6 report recommended the EU open accession talks with Turkey. At the December 17 Summit, the EU is widely expected to follow through on this recommendation by setting a date for talks. This would be a major step forward in anchoring Turkey's future and in our strategic vision for Turkey and the region. However, the GOT is concerned about some of the conditions that may be attached to the EU offer. They worry the EU is still not committed to its membership and continues to raise barriers. For example, the EU is pressing the Turks to sign, before the Summit, a protocol extending the EU Association agreement to the 10 new EU members, including the Republic of Cyprus. GOT officials say they are willing to negotiate on this point, but insist they are not required to sign before beginning accession talks, and they tell us this is presented as a concession to and recognition of the Republic of Cyprus, something they are only willing to see as part of a settlement of the island's division.

110. (SBU) The Turks are also concerned about how the EU will define the "open ended" nature of accession talks. They recognize the successful outcome of the talks cannot be pre-determined. GOT officials say they cannot accept language indicating that Turkey may be offered something less than full membership even if it meets all accession criteria, as some (the Austrians, German CDU leader Merkel) have suggested.

111. (SBU) The EU has indicated that it plans to apply a "screening process" before opening formal talks on each chapter of the EU acquis. The Turks say they can accept this, as long as the screening begins in early 2005 and the formal talks start later in the year. However, they reject any arrangement that would postpone the start of formal talks until 2006.

112. (SBU) Many in Turkey see the U.S. and EU relationships as a zero-sum choice. They believe that relations with the EU can improve by distancing themselves from us. Others also look for a third alternative based on partnership with Russia - which was a theme in the recent Putin visit.

Economy -----

113. (U) The Turkish economy has recovered strongly from the financial crisis of 2000-2001 and is growing at an annual pace of around 10 percent. However, the recovery remains vulnerable due to a large current account deficit (about 5 percent of GDP) and a large debt with a short maturity structure. Some recent data releases and comments by analysts are encouraging on the current account outlook: there are signs the strong growth is decelerating, auto sales are down, and the dollar fall against both the euro and lira is positive for the trade deficit. Macroeconomic success has also bred a sense of complacency about the need to persist with difficult reforms, such as privatization, and reform of the banking, social security and tax systems.

114. (U) Due to historic economic/political volatility and opaque regulatory/judicial systems, Turkey has long received less foreign direct investment than other countries of similar size and potential. Many in the Turkish elite and the GOT are convinced that there will be a flood of foreign investment if the Turks get a date for EU accession negotiations later this month. However, this is unlikely to materialize unless more is done in the area of structural reform. In addition,

there appears to be a lack of appreciation for the enormous challenges Turkey will shoulder in the accession negotiations, for the fact that EU accession will affect nearly aspect of their lives, and that it may in the end be quite costly for Turkey to comply with EU directives in environmental protection and other areas.

IMF

15. (Sbu) At this writing, the GOT is in the thick of negotiations with the current Fund Mission. Though Fund staff told us they would not have come if they did not think they were close enough to agree on the terms of a program by the end of the mission, some politically-difficult issues remain outstanding. Social Security reform, in particular, requires the Prime Minister to approve increases in payroll taxes and/or a later retirement age. On a range of other issues--such as banking law, tax rate details, and out-year fiscal targets--it is not clear how close the two sides are to a deal. Economic technocrats like U/S Canakci have told us they are keen to be able to announce a deal with the IMF before December 17, even if they are not ready to have a signed LOI. Markets are widely-considered to have priced in an IMF deal and a conditional yes from the EU, such that there could be a sell-off if things go worse than expected on either front.

Edelman